Summary of Sections Affecting Individuals

Sec. 1001 Reduction and simplification of individual income tax rates

- The current seven tax brackets would be consolidated and simplified into four brackets: 12%, 25%, 35% and 39.6%, in addition to an effective fifth bracket at 0% in the form of the enhanced standard deduction.
- For married taxpayers filing jointly, the 25% bracket threshold would be $90,000, the 35% bracket threshold would be $260,000, and the 39.6% bracket threshold would be $1 million.
- For unmarried individuals and married individuals filing separately, the bracket thresholds would be half the thresholds for married taxpayers filing jointly, except that the 35% bracket threshold for unmarried individuals would be $200,000.
- For single parents filing as a head of a household, the bracket thresholds would be the midpoint between the thresholds for unmarried individuals and married taxpayers filing jointly, except that the 39.6% bracket threshold for heads of household would be $500,000.
- These income levels would be indexed for chained CPI instead of CPI, a slightly different measure of inflation.

Sec. 1002 Enhancement of standard deduction

- The standard deduction would be increased to $24,000 for joint filers and $12,000 for individual filers.
- Single filers with at least one qualifying child could claim a standard deduction of $18,000.
- These amounts would be adjusted for inflation based on chained CPI.

Sec. 1003 Enhancement of standard deduction

- The deduction for personal exemptions and the personal exemption phase-out would be repealed.

Sec. 1004 Maximum rate on business income of individuals

- Reduces rate for pass throughs to 25% for a portion of their net income, which can be treated as “business income” instead of the individual rate.
- The remaining portion of net business income would be treated as compensation and continue to be subject to ordinary individual income tax rates
- Each owner or shareholder would separately determine their proportion of business income
- Net income derived from a passive business activity would be treated as business income and fully eligible for the 25% max rate.
- Owners or shareholders receiving net income derived from an active business activity (including wages) would determine their business income by reference to their “capital percentage” of the net income from such activities

- **Brady Amendment:** The amendment provides a 9-percent tax rate, in lieu of the ordinary 12-percent tax rate, for the first $75,000 in net business taxable income of an active owner or shareholder earning less than $150,000 in taxable income through a pass-through business.
    - As taxable income exceeds $150,000, the benefit of the 9-percent rate relative to the 12-percent rate is reduced, and it is fully phased out at $225,000.
    - Businesses of all types are eligible for the preferential 9-percent rate, and such rate applies to all business income up to the $75,000 level.
    - The 9-percent rate is phased in over five taxable years, such that the rate for 2018 and 2019 is 11 percent, the rate for 2020 and 2021 is 10 percent, and the rate for 2022 and thereafter is 9 percent.
    - For unmarried individuals, the $75,000 and $150,000 amounts are $37,500 and $75,000, and for heads of household, those amounts are $56,250 and $112,500.
- Under the provision, owners or shareholders may elect to apply a capital percentage of 30% to the net business income derived from active business activities to determine their business income eligible for the 25% rate.
- That determination would leave the remaining 70% subject to ordinary individual income tax rates.
- Owners or shareholders may elect to apply a formula based on the facts-and-circumstances of their business to determine a capital percentage of greater than 30%.
- That formula would measure the capital percentage based on a rate of return (the Federal short-term rate plus 7%) multiplied by the capital investments of the business.
- Once made, the election of the alternative formula would be binding for a 5 year period.
- A special rule would apply to prevent the recharacterization of actual wages paid as business income
- An owner's or sharholder's capital percentage would be limited if actual wages or income treated as received in exchange for services from the pass-through entity exceeds the taxpayer's otherwise applicable capital percentage.
- The determination of whether a taxpayer is active or passive with respect to a particular business activity would rely on current law material participation and activity rules within regulations governing the limitation on passive activity losses under Code section 469.
- Under these rules, the determination of whether a taxpayer is active generally is based on the number of hours the taxpayer spends each year participating in the activities of the business.
- Income subject to preferential rates, such as net capital gains and qualified dividend income, would be excluded from any determination of a business owner's capital percentage.
- Such income would not be recharacterized as business income for these purposes and would retain its character.
- Certain other investment income that is subject to ordinary rates such as short-term capital gains, dividends, and foreign currency gains and hedges not related to the business needs, would also not be eligible to be recharacterized as business income.

- Interest income properly allocable to a trade or business would be eligible to be recharacterized as business income.
- Under the provision, the default capital percentage for certain personal services businesses (e.g., businesses involving the performance of services in the fields of law, accounting, consulting, engineering, financial services, or performing arts) would be zero percent.
- As a result, a taxpayer that actively participates in such a business generally would not be eligible for the 25 % rate on business income with respect to such personal service business.
- However, the provision would allow the same election to owners of personal services businesses to use an alternative capital percentage based on the business's capital investments.
- This election would be subject to certain limitations.
- The provision would also apply a maximum 25 % rate on certain dividends from a real estate investment trust (REIT) and patronage dividends from cooperatives.
- The provision would be effective for tax years beginning after 2017

Sec. 1005 Conforming amendments related to simplification of individual income tax rates

- Makes technical and conforming amendments to the Internal Revenue Code related to reduction and simplification of individual income tax rates.